No. 296

In the Supreme Court of the United States

October Term, 1944

Panhandle Eastern Pipe Line Company, Illinois Natural Gas Company, and Michigan Gas Transmission Corporation, petitioners

v.

Federal Power Commission, City of Detroit, Mich., County of Wayne, Mich., Michigan Consolidated Gas Company, and Michigan Public Service Commission

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE RESPONDENTS

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FEDERAL POWER COMMISSION, CITY OF DETROIT, MICH., COUNTY OF WAYNE, MICH., MICHIGAN CONSOLIDATED GAS COMPANY, AND MICHIGAN PUBLIC SERVICE COMMISSION

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OPINIONS BELOW

The opinion and order of the Federal Power Commission (R. I, 14–43)[1] are reported in 45 P. U. R. (N. S.) 203. The opinion of the Circuit Court of Appeals (R. XVI, 7198–7218) is reported in 143 F. (2d) 488.

[1] In the record citations, roman numerals refer to the volume, arabic numerals refer to the page.

JURISDICTION

The judgment of the circuit court of appeals was entered on June 6, 1944 (R. XVI, 7219-7220). The petition for a writ of certiorari was filed on July 28, 1944. A writ of certiorari was granted on November 13, 1944, limited to Question No. 3 presented in the petition. By order entered January 3, 1945, the scope of review was enlarged to include Question No. 2 presented in the petition. Jurisdiction of this Court rests upon Section 19 (b) of the Natural Gas Act and Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

The questions as to which a writ of certiorari was granted, as stated in the petition and in the order presented in petitioners' brief, are as follows:

(1)[1] Whether the Commission's action in treating petitioners' business as an entirety and refusing to make any allocation or separation with respect to petitioners' regulated and unregulated sales was beyond its statutory power.

(2) Whether limiting the sale price of petitioners' gas for resale so as to provide an over-all return of 6½ percent on the depreciated cost of petitioners' properties including those devoted to production and gathering of natural gas and excluding petitioners' tendered evidence as to

[1] Presented as question (3) in the Petition for Certiorari.

the market value of petitioners' gas leaseholds constituted an exercise of jurisdiction over production and gathering of natural gas in violation of the Natural Gas Act.

STATUTE INVOLVED

The relevant provisions of the Natural Gas Act of 1938 (52 Stat. 821; 15 U. S. C. 717) are set forth in Appendix A, *infra*, pp. 52-67.

STATEMENT

The proceedings before the Commission arose out of a complaint filed February 28, 1941, by the City of Detroit and County of Wayne, Michigan, alleging that the rates and charges of petitioners Panhandle Eastern Pipe Line Company and Michigan Gas Transmission Corporation, for natural gas sold to Michigan Consolidated Gas Company for resale for ultimate public consumption in that City and County, were unjust, unreasonable, and unduly discriminatory (R. XVI, 7002). The Commission, on its own motion, instituted an investigation on May 22, 1941, of all interstate wholesale rates and charges of such petitioners, and later expanded the investigation to include those of petitioner Illinois Natural Gas Company (R. XVI, 7061, 7088). Respondent Michigan Public Service Commission and respondent Michigan Consolidated Gas Company, also urging the propriety of a reduction in the challenged rates and charges, were permitted to intervene in the proceedings, which were consolidated for hearing

(R. XVI, 7024, 7046, 7064). After these proceedings were initiated, petitioner Panhandle Eastern Pipe Line Company acquired all the properties of the other two petitioners, which were then dissolved (Pet. Br. 4, n. 2).

After extensive hearings were had (R. I., 45–R. XVI, 7001) and petitioners' case was closed (R. VIII, 3975, 4011), counsel for Detroit and Wayne County, counsel for the Commission, and counsel for Michigan Consolidated Gas Company, in April 1942, filed separate motions with the Commission requesting an interim order reducing petitioners' rates by $6,800,479, $5,580,888, and $5,489,874 per annum, respectively (R. XVI, 7100, 7104, 7125). Following submission of briefs the Commission, on September 23, 1942, entered its opinion and interim order here under review, finding that petitioners' interstate wholesale rates were excessive and requiring petitioners to reduce such rates on and after November 1, 1942, so that if the reduced rates had been in effect during 1941, there would have resulted a reduction in revenue of $5,094,384 (R. I, 15–37, 38–43).[3]

[3] The Commission's order (R. I, 42) required:

"(A) The rates and charges made, demanded, or received by the respondents for or in connection with their transportation and sale of natural gas in interstate commerce for resale for ultimate public consumption shall be so reduced as to reflect, when applied to respondents' 1941 transportation and sales, a reduction of not less than $5,094,384 per annum below their 1941 consolidated gross operating revenues of $17,789,573 * * *."

The Commission founded its order upon the $78,814,292 actual legitimate cost of petitioners' property in service on December 31, 1941; less $12,596,987 for accrued depreciation, depletion and amortization; plus $920,000 for working capital; which resulted in a rate base of $67,137,305.[4] The Commission allowed a 6½% return on the rate base, which return it found to be "fair and liberal." Using 1941 as the test year, the Commission allowed all operating expenses, including the annual depreciation expense, the exploration and development costs incurred by petitioners in that year as shown by their books, and Federal income taxes (R. I, 30–31).[5] With respect to increases in operating expenses which petitioners claimed would occur after 1941, including increased taxes and amortization of rate case expense, the Commission found, in the light of petitioners' earnings during the first three months of 1942, that these claimed increases in expenses would be more than offset by increased revenues (R. I, 30–33).

Petitioners' application for rehearing (R. XVI, 7141–7149) was denied by the Commission on

[4] There is no dispute as to the actual legitimate cost of petitioners' property (R. I, 21–22; Pet. 8). The amount of accrued depreciation was taken from petitioners' books, as petitioners had requested in their brief before the Commission (R. I, 23). The allowance for working capital was not questioned in the petition for review in the court below (R. I, 6–12).

[5] Two minor adjustments were made, which are not now in dispute (R. I, 30–31).

October 30, 1942 (R. XVI, 7150). Thereafter they filed a petition for review in the circuit court of appeals. That court heard argument on May 14, 1943 (R. XVI, 7196), but deferred its decision pending this Court's disposition of *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591 (R. XVI, 7196). After this Court handed down its opinion in that case on January 3, 1944, the instant case, at the request of the court below, was resubmitted upon supplemental briefs and argument (R. XVI, 7196, 7197), and the court then entered its opinion and judgment on June 6, 1944, affirming the Commission's order (R. XVI, 7198, 7219).

SUMMARY OF ARGUMENT

1. The Commission, in determining the reasonableness of petitioners' interstate wholesale rates under the Act, declined, as unnecessary in the circumstances of the particular case, to make an allocation between petitioners' regulable (interstate wholesale) sales and their non-regulable (interstate direct industrial) sales. The Commission's finding as to the lack of necessity for such an allocation had a substantial basis in the record and was neither arbitrary nor unreasonable. Petitioners' own witness, while presenting an allocation study which segregated the total revenues received from the two classes of business, conceded that his study made no proper allocation of the charges which should be borne by each class, and

while suggesting that a "fair and equitable" allocation could be obtained by crediting to the wholesale business 50% of the apparent profits being derived by the direct industrial sales, he emphasized that the final determination was essentially a matter of "business judgment" to be made by the Commission. Petitioners' president testified that an allocation would be impracticable and unrealistic in view of the unified character of petitioners' business. These views as to the lack of necessity for an allocation were entirely warranted by the fact that petitioners had constructed no capacity for their direct industrial sales, and justified the Commission in treating such sales as a by-product of petitioners' wholesale business.

It may be doubted whether in the light of petitioners' position taken below it is still open to them to argue that nevertheless a formal allocation was essential to the preservation of their rights; but if such a contention may now properly be made, it is without basis in the provisions of the Act. Interstate industrial business is within the Commission's jurisdiction in many respects. It may be conceded that the Commission is without authority to prescribe rates on such business; but here the rate order did not, either in terms or in practical effect, alter petitioners' direct industrial rates. Petitioners under the order are entirely free to raise or lower their direct industrial rates, or maintain them at their 1941 level; and

in the light of this Court's decision in *Lone Star Gas Co.* v. *Texas,* 304 U. S. 224, it is clear that no jurisdictional defect is created by the mere failure to make a formal allocation in respect of the industrial business. The issue is one of confiscation only; and in the light of the liberal return allowed to petitioners by the rate order there is no basis for a claim that the order was in any sense confiscatory.

2. The action of the Commission in reflecting petitioners' production and gathering facilities in the rate base and then limiting the return to 6½% was not a regulation of "production or gathering" forbidden by Section 1 (b) of the Act. That section withholds from the regulatory authority of the Commission the *activity* of producing or gathering natural gas, but there is nothing therein to indicate a Congressional intent to preclude the Commission from considering either such facilities in calculating the rate base or the expenses incident thereto for the purpose of determining the reasonableness of the interstate wholesale rates. *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 614, n. 25. The legislative history of the Act confirms this view. The Committee report, after stating that the negative language in Section 1 (b) was largely surplusage, also stated that the Act contemplated regulation along "more or less standardized lines". The

valuation of production and gathering facilities historically has been an integral part of the regulatory rate fixing procedure. *Dayton Power & Light Co. v. Commission*, 292 U. S. 290.

Sections 6 (a), 6 (b), 8 (a), 9 (a) and 10 (a) of the Act all contain language authorizing the Commission to ascertain the costs of production and gathering facilities. The language and legislative history of Section 14 (b) confirm the view that the Commission is required to investigate such costs. The uniform administrative interpretation of the Commission consistently has been to consider production and gathering facilities in fixing the rate base, and the Commission has so reported to Congress. Finally, legislative approval of the administrative interpretation may be inferred from the fact that when Section 7 was amended in 1942, no legislative change was made in respect of this matter although the Commission's administration of the Act was thoroughly reviewed.

Neither the Commission's refusal to allow the alleged "market value" of petitioners' leaseholds in the rate base nor its failure to calculate costs on a "field" or "commodity" price basis for the natural gas produced by petitioners constituted a deprivation of due process. Evidence of market value of the character offered by petitioners is not compelling or even persuasive. *Dayton Power & Light Co. v. Commission*, 292 U. S. 290, 296–

301. Evidence of field or commodity price of gas is open to the same objections. This is particularly true of the Panhandle and Hugoton fields. The only substantial market is furnished by the large pipelines which fix their own prices, and to speak of commodity value in such circumstances is unrealistic. This Court has recognized the peculiar situation which there obtains in *Thompson v. Consolidated Gas Co.*, 300 U. S. 55. The actual legitimate cost system adopted by the Commission on the other hand is just to consumers and pipelines alike. It considers costs as best calculated to insure continuity in the production of natural gas and the financial soundness of the pipelines themselves. The fact that it has become possible to finance such enterprises at progressively lower rates discloses that the investing public appreciates the ultimate soundness of the Commission's approach.

ARGUMENT

The order of the Commission here under review directed petitioners to reduce their interstate wholesale rates by an amount of not less than $5,094,384 per annum below the 1941 consolidated gross operating revenues of $17,789,573 (R. I, 42). The Commission did not make an allocation of property, profits and expenses, holding that in the peculiar circumstances of this case it was unnecessary so to do. Petitioners, adverting to the fact that their consolidated gross revenues include

profits from both their regulable (interstate wholesale) sales and their non-regulable (interstate direct industrial) sales, contend that, under the statute, the Commission was required to make a formal allocation, supported by detailed findings, of their property, revenues and expenses; that the Commission's action in not doing so is a jurisdictional defect which vitiates the entire rate reduction order; and that the Commission, by considering petitioners' producing and gathering facilities and the expenses incident thereto, exercised a jurisdiction prohibited by Section 1 (b) of the Act.

We submit that, in the circumstances of this case, the Commission's rate reduction order was not arbitrary or unreasonable and that its finding that no allocation was necessary has a substantial basis in the record; that no formal allocation was required in the instant case; and that the Commission was clearly authorized to reflect petitioners' production and gathering facilities in the rate base and to consider the expenses incident thereto.

I

THE COMMISSION'S FINDING THAT NO ALLOCATION WAS NECESSARY IN THE CIRCUMSTANCES OF THIS CASE HAS A SUBSTANTIAL BASIS IN THE RECORD AND WAS NEITHER ARBITRARY NOR UNREASONABLE

The Commission, upon consideration of the evidence with respect to petitioners' regulable

(interstate wholesale) sales and their non-regulable (interstate direct industrial) sales, found that it was "unnecessary to make an allocation" in determining the reasonableness of petitioners' interstate wholesale rates under the Act. We submit that in the circumstances here presented, the Commission's action in this regard was neither arbitrary nor unreasonable.[6]

At the hearing, petitioners presented an allocation study (Exh. 251; R. XIII, 5947–5955) through their witness Biddison,[7] showing that 91.57% of their total revenues, or $16,289,045, was received from their interstate wholesale sales and 8.43%, or $1,500,527, was received from their direct industrial customers (R. XIII, 5947). Of the total operating expenses of $7,425,826, including depreciation, but excluding Federal income taxes and return, this study assigned only $499,-699 to the direct industrial business (R. XIII,

[6] Petitioners, for the first time, contend (Pet. Br. 8, 37) that the Commission erroneously assumed jurisdiction over their wellhead sales to Argus Natural Gas Company. This contention was not advanced in the petition for rehearing (R. XVI, 7147), the petition for review (R. I, 11–12), the briefs below, or the petition for certiorari. Moreover, petitioners' witness Biddison included these sales in his "regulated sales" (R. XIII, 5947, line 7). In any event, the revenue from these sales was negligible, amounting to less than four-tenths of one per cent of petitioners' gross revenues in the test year (See Pet. Br. 37 and R. I, 31).

[7] Biddison's testimony appears at R. VIII, 3631–3676, 3853–3881, 3919–3933.

5947, lines 25–36, incl.). Thus, with revenues of $1,500,527 and assigned operating expenses of $499,699, the direct industrial business was shown to have earned $1,000,828 in the test year, before income taxes (See Pet. Br. 34). The exorbitant margin of profit of more than 200% thus shown[8] on petitioners' direct industrial business was obviously due to the fact that in this study such business had not been assigned its fair share of the cost of transporting gas through the main transmission pipeline.[9]

[8] This result appears all the more incongruous in the light of the fact that petitioners' rates for direct industrial gas in 1941 averaged only 17¢ per Mcf as compared with $1.00 for residential gas, 82.4¢ for commercial gas, and 28.7¢ for gas sold to other utilities (R. XIII, 5947, lines 1–20, incl.). Petitioners sold 1,730,142 Mcf to Missouri Power and Light Co. for boiler fuel at a price of 11¢ per Mcf (R. XIII, 5947).

[9] For example, petitioners did not allocate a single dollar of the main transmission line annual depreciation expense of $2,238,589 to the direct industrial business, but assessed all of such amount to the regulated business (R. XIII, 5955, line 5). Of the ad valorem taxes on the main transmission line, totaling $633,270, only $1,738, applicable to the laterals used exclusively for the direct industrial customers, was allocated to them (R. XIII, 5955). None of the main transmission line operating and maintenance costs was charged to the direct industrial business. For example, the transmission mains operating labor was $288,564, of which only $490 (applicable only to exclusively used laterals) was allocated to direct industrials; the maintenance cost of mains was $94,212, of which only $160 (applicable to exclusively used laterals) was allocated to the cost of conducting the direct industrial business (R. XIII, 5951, lines 15 and 27).

Petitioners' witness recognized that his allocation study would impose an undue burden upon the wholesale business, since virtually all of the main transmission line costs would be saddled upon the domestic and commercial consumers. He admitted that his exhibit did not show the proper charges between the two classes of business (R. VIII, 3856). He testified that a further "step" was necessary to arrive at a fair and equitable distribution of the charges between petitioners' regulable and non-regulable sales. He recommended that a portion of the apparent profit of $1,000,828, shown by his exhibit to have been derived from the direct industrial business, should "as a matter of fairness and equity" be "made a charge against the non-regulated business and substantially paid to the regulated business as a fee for the privilege of using the equipment through which delivery of this non-regulated business is effected." He also emphasized that the determination of what amount should be credited to the regulated business is a matter of "business judgment" for the Commission to decide.[10] He further stated (R. VIII, 3873-3874):

[10] In view of the importance of this testimony, which was quoted only in part in petitioners' brief (p. 33), we set it forth in full at this point (R. VIII, 3856-3857):

"Q. Well, Exhibit No. 251 reflects the manner in which you, in your opinion, believe the allocation of costs should be made, doesn't it?

"A. Yes, when you go to allocating costs and that is all this purports to do, is to allocate the costs. I think there is

"Q. Now, Mr. Biddison, you have testified in many rate cases and I understand it is your opinion that the matter of this further allocation would be a matter of the exercise of enlightened judgment by those

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another step necessary after you have allocated the costs. I have not carried out the other step but it is a matter of business judgment as to how much of profits of the one class of business ought to be paid to the other class, as a matter of fairness and equity, in business judgment.

"Q. Let me see if I understand your last answer. Are you now referring to the allocation of return?

"A. If you take some of the profits from the non-regulated business and credit to the costs of the other business considered as a rental charge for the privilege of using the facilities, you can consider that it has contributed to return and to depreciation.

"Q. I am sorry. I do not quite follow what you have in mind, Mr. Biddison. Maybe if you would explain that in a little different way I might understand you better.

"A. On page 1 of Exhibit No. 251, it is shown that before the modification from proposed new income tax rates at line 42, there is available from these non-regulated sales $651,766.70. Before the income tax of $349,062.28, there was available for income tax and return a little over $1,000,828.98. I think it would be entirely fair and just, in line with what Mr. Goodman commented last week, that some portion of that little over a million dollars should be made a charge against the non-regulated business and substantially paid to the regulated business as a fee for the privilege of using the equipment through which delivery of this non-regulated business is effected. In other words, I think you should first find out how much this non-regulated business is costing and then make some division of the profits from it.

"Now, what that division should be, I think is a matter of business judgment but, in fairness, I think there ought to be some division of it in spite of the fact that the language in the Colorado case does not indicate that to be the view of the Commission."

charged with the duty of making the decisions in this case. Is that right?

"A. That is right, and I further think that they should have the opinion of the experienced management in coming to their final conclusions on that matter."

Upon inquiry by the Trial Examiner as to his own view of a proper division, petitioners' witness expressed the opinion that the $1,000,828 of apparent profits from the direct industrial business (before Federal income tax) should be split "fifty-fifty," stating (R. VIII, 3874):

"* * * In that way, this non-regulated business has contributed half a million dollars a year *towards the reduction in cost of the regulated* business and if it does not contribute something, I do not think there is any justification for having the business." [Emphasis supplied.]

In addition to this testimony by petitioners' witness Biddison, petitioners' president testified that it would be "theoretical", "unrealistic," "not practical", and "a crazy idea" to make a detailed or formal allocation in this case in view of the unified character of the business (R. I, 34; R. VIII, 3960-3962).

In their brief before the Commission, counsel for petitioners requested that the Commission find that petitioners "have built no capacity" for their direct industrial sales, which are "incremental in nature", and that it is "reasonable" to allocate

"50 per cent of the net earnings from nonregulated sales as a credit to net earnings from regulated sales, as compensation for the temporary use of such facilities provided for regulated sales but used from time to time in transporting the gas for direct, interruptible, nonregulated sales, when not required for regulated sales." They requested that the Commission find:

> "27. On the basis of 1941 *pro forma* consolidated revenues, total operating revenues were $17,789,572, of which $16,289,045 are allocable to regulated sales, and $1,500,527 are allocable to nonregulated sales. A credit of $500,414, representing a charge against the nonregulated sales of one-half the profits resultant from such sales, increases total revenues from (and allocable to) regulated sales to $16,789,459." [11]

It was in this setting that the Commission for the reasons stated in its Opinion found that it would be fair and equitable to credit to the wholesale business any earnings of the direct industrial business in excess of a 6½% return for the use of the main transmission line facilities. Stated another way, the incidental direct industrial business was treated as a "by-product of the wholesale business, comparable to [petitioners'] gaso-

[11] Sec. 50.68 of the Commission's Rules and Regulations Under the Natural Gas Act provides that briefs "should include requests for such specific findings as the party thinks the Commission should make." 18 CFR (1943 Supp.) 4539.

line extraction business" (R. I, 34).[12] In such circumstances, it was, of course, unnecessary to make any formal or detailed allocation, and the Commission so held (R. I, 33–34).

We submit that in view of the foregoing there is no basis for any contention that the Commission's finding that no allocation was necessary represented arbitrary or unfair action.

Petitioners, however, seek to escape the effect of Biddison's testimony (Pet. Br. 30, 32–34). Although we have difficulty following the ramifications of petitioners' calculations and statements by which such conclusion is sought to be reached (Pet. Br. 32–34), it appears that they now contend that they are entitled to the \$319,656 of apparent earnings on direct industrial sales in *addition* to the 6½% return fixed by the Commission on the entire business. Thus, petitioners seek to lay a basis for the claim that they were "deprived" of \$319,656 by the Commission's action. This contention has no foundation in the record, is contrary to Biddison's testimony (R. VIII, 3857, 3872–3874) and represents a complete shift of

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[12] Petitioners agreed in the hearing that the expenses and revenues in connection with the sale of gasoline extracted from the natural gas should be treated in like manner, i. e., as an integral part of petitioners' entire operations (R. I, 34). No contention has been advanced by petitioners that by so doing the Commission was exercising jurisdiction over their gasoline sales.

position from that taken by petitioners before the Commission.[13]

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[13] In their principal brief before the Commission, petitioners stated (pp. 72-73):

"Application of Biddison's recommendation. Witness Biddison explained that Exhibit 251 was prepared for the purpose of determining the 'cost' to Respondents [petitioners] of the gas service subject to regulation and that not regulated; but that, with certain adjustments, *it could be used for a determination of the 'profit' earned from nonregulated sales of gas*, one-half of which he thought might well be credited to the regulated part of the business as a carrying charge for the use of facilities provided for that regulated business and used for unregulated service only to the extent not required and when not required for the regulated gas. [Emphasis supplied.]

"Earnings before Federal taxes. He explained that by the addition of lines 38 and 42, columns E and F, page 1 of that exhibit, it was disclosed that earnings before Federal taxes were $8,863,218 from sales of regulated gas and $1,000,828 from sales of the nonregulated gas—a total of $9,864,046. It was his business judgment that one-half these earnings of $1,000,828 (or $500,414) should be credited to the regulated gas as a carrying cost or charge. This would result in a *total earning* before such Federal taxes of $9,363,632 from the regulated gas and $500,414 from the nonregulated gas, the proportions of the total being 94.92 per cent and 5.08 per cent respectively. [Emphasis supplied.]

"Application of Federal income and excess profits taxes. Witness Biddison stated that after making this computation the approximate income and excess profits taxes should be applied proportionally to the earnings of the respective classes of sales, since it is earnings which fix the amounts of such taxes. The total tax payable on these earnings being $3,558,228, that sum may therefore be allocated between the earnings from regulated sales and earnings from nonregu-

It is thus apparent that the Commission's finding that no allocation was necessary in the circumstances of this case has a substantial basis in the record and was neither arbitrary nor unreasonable. Due process requires no more.

II

THE ABSENCE OF A FORMAL ALLOCATION IN THE INSTANT CASE DOES NOT INVALIDATE THE COMMISSION'S ORDER

The absence of a formal allocation in the instant case is not a jurisdictional defect, and the rate reduction order, being addressed to interstate sales for resale only, is to be tested by the ordinary criteria as to whether the rates prescribed were confiscatory *vel non*.

A. ALLOCATION IS NOT A JURISDICTIONAL REQUIREMENT

At the outset, it is to be noted that the Act does not in terms require an allocation, although it must have been a matter of common knowledge that the majority of the companies subject to the

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lated sales, and the net operating revenues may thus be determined as follows:

	Regulated Sales	Non-regulated Sales
Indicated earnings before taxes	$9, 363, 632	$500, 414
Taxes (aggregating $3,558,228)	3, 377, 470	180, 758
Net Operating Revenues	5, 986, 162	319, 656"

jurisdiction of the Commission in respect to their interstate sales for resale also had intrastate sales and direct interstate industrial sales. Congress rather obviously left the problem of allocation to the expert judgment of the Commission. This it was at liberty to do, for it is clear that Congress could have provided for the same regulation over direct industrial sales as it did for interstate sales for resale. In any event we submit that allocation is not a jurisdictional requirement in the instant case, as the Act does not leave the interstate direct industrial sales wholly unregulated [14] and the rate order here under review neither operated nor purported to operate upon the direct sales.

1. *Jurisdiction over the direct industrial business of a natural gas company is not entirely withheld from the Commission.* While it may be conceded that the Commission has no authority to fix rates for direct industrial sales (see *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 615–616), it does possess certain regu-

[14] There is nothing to indicate that the states have any jurisdiction over interstate direct industrial sales of gas and we do not understand petitioners to contend or suggest that their direct industrial sales are subject to state regulation. Such sales are made pursuant to contract and not under rates in which there might conceivably be some matter of local concern. Compare *Pennsylvania Gas Co.* v. *Public Service Commission*, 252 U. S. 23, 30–31, with *Missouri* v. *Kansas Gas Co.*, 265 U. S. 298, 307–309.

latory powers in respect of that phase of the business of a natural gas company. Section 1 (a) of the Act, *infra*, p. 52, declares "that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest." It is, of course, clear that the direct industrial business involved in the instant case comprises both interstate transportation and interstate sales. Section 4 (c) of the Act requires the filing with the Commission not only of all schedules embodying rates and charges subject to the jurisdiction of the Commission and the classification practices and regulations affecting such rates and charges, but also "all contracts which in any manner affect or relate to such rates, charges, classifications and services." Contracts for direct interstate industrial sales of course come within Section 4 (c).[15] Section 5 (a) of the Act authorizes the Commission either upon complaint or upon its own motion to investigate and determine whether any rate or charge subject to the jurisdiction of the Commission "is unjust, unreasonable, unduly discriminatory, or preferen-

[15] By Rule 54.30 of its Rules and Regulations Under the Natural Gas Act the Commission requires the filing of all contracts for direct industrial sales which involve sales in excess of 100,000 M. C. F. per year (7 Fed. Reg. 4824). The contracts involving petitioners' direct sales have been filed with the Commission.

tial,'' or whether "any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential." Inasmuch as the matters subject to the control exercised under Section 5 (a) are by the terms of the Act coextensive with those included in Section 4 (c), it follows that contracts covering direct sales in interstate commerce are not entirely outside the scope of the Act.

Petitioners' contentions that their interstate direct industrial business was to be entirely free of regulation is not persuasive (Br. 19–21).[16] They overlook the fact that Section 1 (b) makes the provisions of the Act applicable "to the transportation of natural gas in interstate commerce," and incorrectly state (Br. 19) that the section makes the provisions of the Act applicable only to the transportation and sale in interstate commerce of natural gas for resale. They rely upon the legislative history of H. R. 11662, which was not the bill enacted and which specifically excluded from the jurisdiction of the Commission authority to fix rates and charges "for the sale of natural gas

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[16] The assertion of petitioners that it is immaterial whether the business "not subject to regulation by the Commission" is operated at a loss or at high profit (Br. p. 21) finds no foundation in the Act. A loss might burden the "regulated" business and a high profit might well be evidence that the "unregulated" business is not bearing its proper share of the costs.

for industrial use only." [17] No such provision appears in the Natural Gas Act.

2. *The rate reduction order of the Commission did not, either in terms or in effect, alter the direct industrial rates.* The order of the Commission directed petitioners to reduce their rates and charges for their interstate sales for resale for ultimate public consumption, effective as of November 1, 1940, so as to reflect, when applied to petitioners' 1941 transportation and sales, a reduction of not less than $5,094,384 per annum below their 1941 consolidated gross operating revenue of $17,789,573. Concededly the Commission, in thus determining what would be a just and reasonable rate on petitioners' wholesale business, considered their entire consolidated income available for return, including income from direct industrial sales. But the Commission's order operates prospectively. As to the years in which it is in effect, it prescribes merely that rates on sales for resale shall be maintained at a given level. This level was calculated on the basis of

[17] Thus, in reporting H. R. 11662, the Committee report stated (H. Rep. 2651, 74th Cong., 2d Sess., p. 1): "The sale of natural gas for industrial use only is also exempted from the jurisdiction of the Commission." In H. R. 6586, which emerged as the Natural Gas Act, no such language appeared in Section 1 (b) and both the House and Senate reports significantly refrained from making any such assertion. H. Rep. 709, 75th Cong., 1st Sess.; S. Rep. 1162, 75th Cong., 1st Sess.

a specified rate of return (6½%) for the test year on petitioners' entire business, but the order, even though based on such a rate of return, in no way fixes the rate of return which may be earned by petitioners during the years in which they may operate under the order. They are merely required to maintain their resale rates at the level fixed; they may vary their industrial rates as they will, up or down, or leave them the same; and they may earn such a return on their business, both direct industrial and resale, as business conditions and the effectiveness of their management will allow. The order, therefore, not only falls short of directly regulating their rates on industrial business; it does not even regulate such rates indirectly by limiting the return which may be secured from such business.

3. *An allocation is not required merely because a portion of an integrated utility's operations is not subject to the Commission's jurisdiction.* This precise question was before this Court in *Lone Star Gas Co.* v. *Texas,* 304 U. S. 224. There the Railroad Commission of Texas had issued an order requiring a reduction in the rates charged in Texas by the company, which operated an integrated production, gathering and transmission system for the sale of natural gas

in Texas and Oklahoma. The State Commission had treated the system as a unit in establishing a rate base and had made no allocation of the company's property, profits and expenses (304 U. S. at 227, 239, 241). In a suit to enforce the order, the state court had directed that a segregation of property between intrastate and interstate functions be made. The Court of Civil Appeals for the Third Judicial District of Texas reversed the lower court but affirmed its holding that it was necessary to allocate or segregate the property used in Texas. This Court, after holding that "The Commission did not attempt to regulate the interstate transportation of gas" nor the "sales and deliveries of gas in interstate commerce" (304 U. S. at 236), stated (p. 241):

> We think that this ruling as to the necessity of segregation, and that the sufficiency of appellant's evidence should be determined by that citerion, was erroneous. This was not a case where the segregation of properties and business was essential in order to confine the exercise of state power to its own proper province. Compare *Smith* v. *Illinois Bell Telephone Co.*, 282 U. S. 133, 148, 149.

Similarly the order of the Commission here did not operate upon any rates other than those for resale. The decision in the *Lone Star* case demonstrates, we submit, that there was no juris-

dictional necessity in such a situation for making an allocation.[18]

It is thus clear that in this, as in other judicial reviews of rate reduction orders, the essential question is that of confiscation. *Railroad Commission* v. *Pacific Gas Co.*, 302 U. S. 388, 394; *Federal Power Commission* v. *Natural Gas Pipeline Company*, 315 U. S. 575, 585. Where certain of the interstate rates of a natural gas company are not subject to regulation by the Commission, but the order of the Commission is directed exclusively to those rates over which it has jurisdiction, the purpose to be served by an allocation is clear. The allocation between the regulable and non-regulable sales assists the Court in determining on review whether the prescribed rates violate constitutional standards. *Banton* v. *Belt Line Ry. Corp.*, 268 U. S. 413; *Wabash Val-*

[18] The contention of petitioners (Br. 39), also vigorously urged by petitioners in *Canadian River Gas Co.* v. *Federal Power Commission*, No. 380 (Pet. Br., pp. 72–75), that a segregation or allocation of physical property is required is without merit. Whatever current vitality the *Minnesota Rate Cases*, 230 U. S. 352, 435, and *Smith* v. *Illinois Bell Telephone Co.*, 282 U. S. 133, 150, now possess in respect of a state regulatory body's failure to segregate physical property when the question of state regulation of interstate commerce is concerned (but see *Lone Star Gas Co.* v. *Texas*, 304 U. S. 224, 239, 241), the rule is well settled that in cases not involving any such conflict of jurisdiction a fair division of costs alone is adequate. *Banton* v. *Belt Line Ry. Corp.*, 268 U. S. 413, 421; *Wabash Valley Elec. Co.* v. *Young*, 287 U. S. 488, 498–500; cf. *Houston* v. *Southwestern Tel. Co.*, 259 U. S. 318, 322–323.

ley Elec. Co. v. *Young*, 287 U. S. 488, 497–498. It is in this light, we submit, that the question of the necessity of an allocation must be approached.[19]

B. THERE WAS NO CONFISCATION

In the instant case, there is no significance to the fact that the amount of the reduction in petitioners' interstate wholesale rates was measured by the difference between their total revenues and a fair return on all their properties. It was petitioners' resale rates alone which were directed to be reduced. Petitioners now contend that in the test year they were actually earning in excess of a 6½% return on their direct industrial sales, and that this return cannot be maintained under the rates fixed by the Commission without reducing

[19] While a failure to make a suitable allocation or allowance of costs in an appropriate case may be a denial of due process (cf. *Banton* v. *Belt Line Ry. Corp.*, 268 U. S. 413, 421; *Columbus Gas Co.* v. *Commission*, 292 U. S. 398, 404–405; Beutel, *Valuation As A Requirement Of Due Process*; 43 Harv. L. R. 1249, 1268–1274), petitioners are in no position here to claim a denial of due process, since the Commission's finding that an allocation was unnecessary was based upon the testimony of petitioners' own witnesses. See *supra*, pp. 12–16. Where factors are present which indicate that an allocation is appropriate, as in *Colorado Interstate Gas Co.* v. *Federal Power Commission*, *Canadian River Gas Co.* v. *Federal Power Commission*, and *Colorado-Wyoming Gas Co.* v. *Federal Power Commission*, Nos. 379, 380 and 575, this Term, the Commission makes an allocation. The "broad distinction" between those cases and the case at bar was explicitly recognized by petitioners' witness Biddison, who testified that the lack of provision of capacity for petitioners' industrial customers justified a different treatment (R. VIII, 3868–69).

below 6½% their rate of return on their interstate wholesale business. Even assuming that in the light of their position taken at the hearing petitioners are now free to advance this contention, the conclusion of confiscation does not follow. It cannot seriously be contended that a return of 6½%, which the Commission here found to be "fair and liberal" for purposes of this interim order (R. I, 30), is the lowest possible permissible rate of return (see Hearings, Committee on Interstate and Foreign Commerce, on H. R. 4008, 75th Cong., 1st Sess., p. 35). The Commission's return, computed at 6½% on the rate base of $67,137,305, amounted to $4,363,925. Even if this return were reduced by $331,000 (the maximum amount of which the petitioners claim (Pet. Br. 33–36) they were "deprived"), the remaining return would be $4,032,925, slightly in excess of a 6% rate of return on the over-all rate base. In this connection, it may be noted that this Court has found no constitutional difficulty with a rate of return for a natural gas utility of 6 per cent. *Lone Star Gas Co.* v. *Texas*, 304 U. S. 224. We, accordingly, submit that no allocation is required in the instant case to aid the Court in determining whether the rate reduction order resulted in confiscation.

The end result of the Commission's order "viewed in its entirety" is not "unjust and unreasonable" under the standards laid down by this Court. *Federal Power Commission* v. *Hope Nat-*

ural Gas Co., 329 U. S. 591, 602; *Federal Power Commission v. Natural Gas Pipeline Company*, 315 U. S. 575, 585–586. The Commission's rate order allowing the 6½% return on the rate base will permit petitioners to earn $4,363,925 upon the basis of the test year after meeting all operating expenses, including annual depreciation expenses, exploratory and development costs, and Federal income taxes (R. I, 30). The undisputed annual cost of servicing petitioners' long-term debt is $957,786 (or 2.88%) and the cost of servicing the preferred stock is $939,000 (or 5.8%), a total of $1,896,786 (R. XIV, 6097), which leaves $2,467,-139 for petitioners' $20,184,175 of common stock, a return upon such stock of 12% (R. XII, 5501). Assuming even that petitioners are entitled to a return on their surplus, the earnings of $2,467,-139 would provide a return of 9 per cent on the combined common stock and surplus of $27,650,-000 (R. XII, 5501). The allowed rate of return, as the Commission found (R. I, 28–30), is commensurate with the returns on investments in other enterprises having corresponding risks and is more than sufficient to insure confidence in petioners' financial integrity. There is thus no room for any contention that the rate afforded petitioners is "unjust and unreasonable." Cf. *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U. S. 575, 586.

III

THE COMMISSION DID NOT EXCEED ITS JURISDICTION WITH RESPECT TO PETITIONERS' PRODUCING AND GATHERING FACILITIES

Petitioners contend that the Commission was under a statutory duty by reason of Section 1 (b) of the Act to eliminate petitioners' producing and gathering facilities from the rate base, to disallow expenses of producing and gathering, and in lieu thereof, to allow a so-called "field price" for the gas produced by petitioners (Pet. Br. 48). We submit that, as this Court held in *Federal Power Commission v. Hope Natural Gas Co.*, 320 U. S. 591, 614, n. 25, there is no merit in this contention, which was raised for the first time in this proceeding in the reply brief which petitioners filed in the court below.[20] While it is clear that under Section 1 (b) of the Act the Commission has no jurisdiction to regulate "production and gathering" as such, the Commission, in determining the reasonableness of a natural gas company's interstate wholesale rates, properly reflects its production and gathering facilities in

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[20] In the proceedings before the Commission, petitioners admittedly "did not attempt" to segregate their producing and gathering properties or the expenses incident thereto (Pet. Br. 49); nor did petitioners raise the objection in their petition for rehearing (R. XVI. 7141-7148), as required by Section 19 (b) of the Act, or in their petition for review in the court below (R. I. 1-44).

the rate base, and properly considers the expenses, including depletion, incident thereto. This is apparent from the purposes and provisions of the Natural Gas Act, as well as its legislative history.

Section 1 (a) of the Natural Gas Act declares that "Federal regulation *in matters relating to* the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest" (emphasis supplied), and in accordance with this declaration of policy, Section 1 (b) provides that the Act "shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale."

As petitioners tacitly recognize (Pet. Br. 46), the above quoted provision in Section 1 (b), considered alone, clearly vests the Commission with jurisdiction over the production and gathering facilities of a natural-gas company. Petitioners contend, however, that the Act as a whole indicates that Congress intended to exclude from regulation the production and gathering phase of the business of a natural-gas company. In support of this contention petitioners principally rely upon the "but" clause in Section 1 (b), which specifies that the Act "shall not apply to any other transportation or sale of natural gas or to the local

distribution of natural gas or to the facilities used for such distribution or *to the production or gathering of natural gas*" (emphasis supplied).

At the outset, it may be conceded that Section 1 (b) withholds from the regulatory power of the Commission the *activity* of producing or gathering natural gas, and that accordingly the Commission has no authority over such matters as, for example, the determination of the drilling or spacing of wells in the field, the number of wells to be drilled in a common reservoir, proration of the production of oil or gas, or cycling or other recovery operations. However broad may be the catalogue of activities thus excluded from the Commission's jurisdiction, we submit that there is no warrant for assuming that Congress, by excluding such activities, intended to preclude the Commission from reflecting the production and gathering facilities of a natural-gas company in the rate base and considering the expenses incident thereto for the purpose of determining the reasonableness of interstate wholesale rates under the Act.

The legislative history confirms the fact that the "but" clause in Section 1 (b) does not remove from the Commission's jurisdiction what would otherwise be subject thereto by reason of its authority over the transportation and sale of natural gas in interstate commerce for resale under the first part of Section 1 (b). Thus, the House

Committee on Interstate and Foreign Commerce in reporting the bill (H. R. 6586, 75th Cong., 1st Sess.) which became the Natural Gas Act, quoted the "but" clause in its report (H. Rep. No. 709, 75th Cong., 1st Sess., p. 3) and then stated:

> "*The quoted words are not actually necessary,* as the matters specified therein could not be said fairly to be covered by the language affirmatively stating the jurisdiction of the Commission, but similar language was in previous bills, and, rather than invite the contention, however unfounded, that the elimination of the negative language would broaden the scope of the act, the committee has included it in this bill. That part of the negative declaration stating that the act shall not apply to 'the local distribution of natural gas' *is surplusage* by reason of the fact that distribution is made only to consumers in connection with sales, and since no jurisdiction is given to the Commission to regulate sales to consumers the Commission would have no authority over distribution, whether or not local in character." [Emphasis supplied.]

Section 5 (a) of the Act places the duty upon the Commission to determine "the just and reasonable rate, charge * * * to be thereafter observed and in force, and * * * fix the same by order." In both *Federal Power Commission* v. *Natural Gas Pipeline Co.,* 315 U. S. 575, and *Federal Power Commission* v. *Hope Natural Gas*

Co., 320 U. S. 591, the Commission, without challenge by either the natural-gas companies or this Court, included the production and gathering facilities in the rate base on which a return was allowed. Indeed, in the *Hope* case, this Court observed (320 U. S. 616) that the Natural Gas Act contemplated "regulation along recognized and more or less standardized lines", citing H. Rep. 709, *supra*, p. 3. The valuation of production and gathering facilities historically has been an integral part of the regulatory procedure in fixing rates for natural gas. *Dayton Power & Light Co.* v. *Commission*, 292 U. S. 290; *Lone Star Gas Co.* v. *Texas*, 304 U. S. 221.

There are numerous provisions in the Natural Gas Act which clearly indicate that the Commission has jurisdiction over the production and gathering properties of a natural-gas company to the extent necessary to carry out its functions under the Act and particularly its principal function of determining the reasonableness of the company's interstate wholesale rates. Thus, Section 6 (a) authorizes the Commission to "investigate and ascertain the actual legitimate cost of the property of every natural-gas company, the depreciation therein, and, when found necessary for rate-making purposes, other facts which bear on the determination of such cost or depreciation and the fair value of such property." Section 6 (b)

requires every natural-gas company, upon request, to file with the Commission "an inventory of all or any part of its property and a statement of the original cost thereof." It will be noted that Section 6, which is directly related to the Commission's rate-making powers, extends to all the property of a natural-gas company. Similarly, Section 8 (a), in authorizing the Commission to prescribe uniform and correct accounting for natural-gas companies, extends to all the property of such companies.[21] And under Section 9 (a), the Commission is authorized to determine and to fix by order the proper and adequate rates of depreciation and amortization "of the several classes of property of each natural-gas company used or useful in the production, transportation, or sale of natural gas." That the Commission's authority under this section is directly related to its rate-making powers is indicated by the proviso that nothing in that section shall limit the power of a state commission to determine the rates of depreciation or amortization to be allowed for the purpose of determining rates or charges subject to state regulation. Under Section 10 (a) the Com-

[21] Section 8 (a) of the Natural Gas Act is identical with and was taken from Section 301 (a) of the Federal Power Act. In reporting out the latter, the Senate Committee on Interstate Commerce stated (S. Rep. No. 621, 74th Cong., 1st Sess., p. 53) that "the authority of the Commission over the accounts of companies under its jurisdiction extends to the entire business of such companies."

mission is authorized to require natural-gas companies to file reports giving full information as to assets and liabilities as well as the cost of maintenance and operation "of facilities for the production, transportation, or sale of natural gas." [22]

The conclusion that Congress contemplated that the Commission would consider the production and gathering properties of a natural-gas company in determining interstate wholesale rates, is reinforced by the provisions and legislative history of Section 14 (b) of the Act. That section authorizes the Commission, after hearing, to determine the adequacy or inadequacy of the gas reserves of natural-gas companies, and, also after hearing, to "determine the propriety and reasonableness of the inclusion in operating expenses, capital, or surplus of all delay rentals or other forms of rental or compensation for unoperated lands and leases." The section further provides that the Commission, for purposes of such determinations, may require each natural-gas company to file copies of "all its lease and royalty agreements with respect to such gas reserves."

The direct relation of Section 14 (b) to the Commission's rate-making authority is clearly

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[22] Section 5 (b) further provides that the Commission "may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas."

indicated by its legislative history. As introduced, the bill (H. R. 4008, 75th Cong., 1st Sess.) which, as amended (H. R. 6586, 75th Cong., 1st Sess.), became the Natural Gas Act, did not contain the provisions of Section 14 (b).[23] In the hearings before the House Committee the National Secretary of the Cities Alliance urged that the provisions of Section 14 (b) be added to the bill, "to prevent great pipe-line corporations from acquiring more acreage than is necessary to supply the consuming public which it serves, and so far as the proposed amendment is concerned, would keep them from passing on the charge of carrying that property to the consuming public." He recognized that he could not ask the Committee "to go so far as to prevent them from making the purchase, if they want to, but we can ask that provision can be made whereby the Commission can see that the cost of carrying those excess acres, that are not necessary in the public interest, shall not be taken into consideration in passing upon the question of what are proper rates to be charged the consuming public" (Hearings on H. R. 4008, 75th Cong., 1st Sess., pp. 60, 67, 84).

The purpose of Section 14 (b) is further apparent from the testimony of Mr. William A. Dougherty before the Committee. Mr. Dougherty,

[23] The provisions of Section 14 (b) were contained in another bill (H. R. 5711, 75th Cong., 1st Sess.) which the Committee then had before it in addition to H. R. 4008.

who identified himself as a New York attorney connected with the management of certain natural gas pipe-line companies, including Colorado Interstate Gas Company (Petitioner in No. 379, this Term), which he named (Hearings, p. 123), objected to the proposed amendment because of the additional expense which would be involved in filing copies of all leases and royalty agreements. He contended that such a requirement was "not necessary" since the "only purpose of having information on lease and royalty agreements is when you are determining a rate and when you are going to determine a rate you can have those things brought in" (Hearings, p. 131). Mr. Dougherty further stated that careful consideration should be given to the provisions of the proposed amendment authorizing the Commission to determine the adequacy or inadequacy of gas reserves, and pointed out that "the Commission can exclude carrying charges of vast amounts of reserves as charges that have no immediate bearing on the immediate rate" (Hearings, p. 132). He added that "the law already gives the Commission the right to exclude delay rentals if the Commission feels that the reserve for which the delay rentals are included are too extensive, and I think the Commission would have that right even without this wording with respect to determining the adequacy or the inadequacy of gas reserves" (Hearings, pp. 132–133).

The hearings which the House Committee on Interstate and Foreign Commerce held on the first predecessor bill (H. R. 11662, 74th Cong., 2nd Sess.) which was reported out (H. Rep. 2651, 74th Cong., 2nd Sess.) confirm the Commission's view. There the then Solicitor of the Federal Power Commission, Dozier A. DeVane, agreed with a member of the committee that the Commission "would go into all the great natural gas fields of this country to determine costs" and "ascertain the cost of generating plant, and all the facilities, and, of course, build up a proper foundation for your rate finally to be sustained" as was done under Title II of the Federal Power Act (Hearings, pp. 31-32).

In addition, the Commission's administrative interpretation of the Act in this connection is of particular significance since it has been impliedly approved by Congress. The Commission in determining the reasonableness of interstate wholesale rates has consistently reflected the company's production and gathering facilities in the rate base.[21] This administrative interpretation

[21] *Illinois Commerce Comm.* v. *Natural Gas Pipeline Co.*, 35 P. U. R. (N. S.) 41, affirmed 315 U. S. 575; *Re Lone Star Gas Co.*, Order of May 4, 1942, in Docket No. G-209; *Cleveland* v. *Hope Natural Gas Co.*, 44 P. U. R. (N. S.) 1, affirmed 320 U. S. 591; *Re El Paso Natural Gas Co.*, Order of October 29, 1942, in Docket No. G-257; *Re Northern Natural Gas Co.*, 47 P. U. R. (N. S.) 74.

of the Act was brought to the attention of Congress in the Commission's Twentieth Annual Report for the year 1940, which summarized the Commission's work in connection with major rate cases and in so doing, stated (p. 77):

> *Gas reserves.*—As the natural-gas industry is an extractive industry, *one of the important elements of cost which must be determined pertains to the exhaustion of the service life of the properties due to the depletion of the natural-gas reserves which the properties were constructed to produce or transport.* The Commission's geologists have been engaged in estimating the volume of gas reserves in a number of important fields, among them the Panhandle field in Texas, the Hugoton field in Kansas and a major portion of the fields located in West Virginia, Pennsylvania, and New York. A few years' difference in the estimated life of available gas reserves supplying a given market may *make a large difference in the rates* which can be justified for that area. [Emphasis supplied.] [25]

Soon after this report was submitted, the House Committee on Interstate and Foreign Com-

[25] The report also pointed out that the Commission's staff, in connection with the organization of natural gas rate cases "along the lines indicated", had made four comprehensive field investigations, including the "Canadian River Gas Co., Colorado Interstate Gas Co., and Colorado-Wyoming Gas Co. in the Mid-West," the proceedings now under review in Nos. 379, 380 and 575, this Term.

merce held hearings on a bill (H. R. 5249, 77th Cong., 1st Sess.) to amend Section 7 of the Natural Gas Act to broaden the Commission's jurisdiction with respect to certificates of public convenience and necessity. Following extensive hearings, during which the Commission's administration of the Act was fully explored (see Hearings pp. 34–35, 40–46, 60–61), the bill was favorably reported and enacted on February 7, 1942.

We accordingly submit that the Commission had jurisdiction to reflect petitioners' producing and gathering facilities in their rate base, and to consider the expenses incident thereto in determining the reasonableness of their interstate wholesale rates. And the contention to the contrary which petitioners now advance therefore furnishes no support to their claim that the Commission should have found and allowed a so-called "field price" for the gas which they produce.

IV

IN DETERMINING THE REASONABLENESS OF PETITIONERS' INTERSTATE WHOLESALE RATES THE COMMISSION IS NOT REQUIRED TO VALUE THE GAS WHICH THEY PRODUCE ON THE BASIS OF A "FIELD PRICE"

Petitioners contend that the Commission's failure to determine and allow a so-called "field price" for the gas which they produce "was arbitrary, discriminatory, lacking any rational basis and

amounted to a denial of due process" (Pet. Br. 54). They also contend that a second approach which substantially would have achieved the same result—including leaseholds in the rate base at their market value—was also improperly rejected by the Commission (Pet. Br. 49). We submit that these contentions, not being supported by the alleged absence of jurisdiction over production and gathering facilities (pp. 31-42, *supra*), resolve themselves into the sole question of whether the "end result" of the Commission's rate order is confiscation (*Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 602) and this Court did not grant review of that question presented in the petition (p. 3).

In any event, petitioners' contention (Pet. Br. 52) that its leaseholds "can be sold" for more than $8,000,000 is based upon the opinion evidence of their own witness. The "value" ranging from $100 to $5 per acre (R. IX, 4199) which this witness assigned to the leaseholds reflected the assumed "value" from the demand for gas by petitioners' customers and the construction of pipeline facilities to serve them (R. IX, 4192). Such "value" was also enhanced by the benefits of conservation legislation (R. IX, 4193). This was thus the same type of testimony which this Court condemned in the *Dayton Power & Light Company* case (292 U. S. 290, 299):

> * * * But plainly opinions thus offered, even if entitled to some weight, have

no such conclusive force that there is error of law in refusing to follow them. This is true of opinion evidence generally, whether addressed to a jury [cases cited] or to a judge [cases cited] or to a statutory board [cases cited]. There are reasons why the principle has special application here. In the first place, the intrinsic value of the leases is dependent upon the capacity of the lands to yield productive wells, a capacity seldom to be judged with even a fair approach to certainty until tested by experience. *Natural Gas Co. of W. Va.* v. *Public Service Comm.*, 95 W. Va. 557, 569, 121 S. E. 716. In the second place, the profits to be earned in a regulated business must vary with the rates established by the supervising agencies of government, with the result that prophecies, however radiant, may be upset over night by the publication of a lower schedule.

Obviously, testimony of such a character is not so compelling as to require the Commission to disregard the actual legitimate cost of the properties involved.

As indicated in petitioners' brief (pp. 53–54), there is no essential difference between petitioners' claim of a so-called "field price" for the natural gas which they produce and their claim of the "market value" of their leaseholds. While evidence as to field price is subject to the same infirmities as were attributed in the *Dayton* case to

evidence of market value, the vice of the "field price" test lies even deeper.

The only substantial markets for gas in large reserves, such as the Hugoton and Panhandle fields, are located at points distant from the fields, and in order to transport gas to these markets it is necessary to construct expensive pipe lines.[26] Before embarking on such an undertaking, it is essential that the company constructing the line be assured of an adequate supply of gas. This is accomplished either by acquiring sufficient producing and proved gas acreage to insure future supplies, or by entering into long-term contracts with producers of gas under which the parties are bound to the sale and purchase of the gas as long as it shall be produced in paying quantities. Federal Trade Commission Report pursuant to Senate Resolution No. 83, 70th Cong., 1st Sess., Vol. 84-A, pp. 70 *et seq.* In a sense the cost which the pipeline company will be required to pay for the natural gas is determined at the inception of the enterprise. In a setting such as this the concept of a "field" or commodity price is unrealistic.

This Court had occasion to review the situation which obtains in the Panhandle field in *Thompson* v. *Consolidated Gas Co.*, 300 U. S. 55. Without access to pipelines and their distant

[26] E. g., petitioners' pipeline represented an investment in excess of $70,000,000 (R. XII, 5527); Natural Gas Pipeline Co. had a book cost in excess of $60,000,000 (315 U. S. at 579).

markets, natural gas produced in the fields had no commercial value other than the extraction of natural gasoline or the production of carbon black (id., pp. 59, 70). In the *Thompson* case, this Court held unconstitutional a Texas statute which sought to compel large pipeline companies to purchase a part of their gas requirements from private producers. There the question of commodity price was not even reached—the pipeline companies did not want the gas at any price.

The value which gas obtains in a market such as the Panhandle or Hugoton field depends exclusively upon the price which the few large pipeline companies are willing to pay. Cf. *United Fuel Gas Co. v. Railroad Commission*, 278 U. S. 300; *Dayton Power & Light Co. v. Commission*, 292 U. S. 290, 301. Whatever might be the situation where the demand equals or exceeds the supply of natural gas, it is apparent that where the market can absorb only a small fraction of the gas produced the purchaser is in a superior bargaining position. In such circumstances the commodity price, if the law of supply and demand is permitted to operate, will necessarily tend to reflect cost alone. And should competition be sufficiently keen, that cost would probably not carry a 6½% profit.[27] Were petitioners deprived of their markets outside the state, their gas would have little if any value.

[27] The Commission, in fixing costs in the instant case, included therein a return of 6½% on the rate base.

Prevailing prices accordingly do not establish a commodity value. When the sales contracts extend for the life of the wells, and vary among themselves, the rates fixed therein merely reflect what the parties to the contract at one time considered to be a fair price. It could currently be either more or less. There is no such thing as a true commodity price unless there are frequent adjustments in price to reflect the changing supply and demand. Moreover, the adoption of a commodity price would open the door for the establishment of fictitious prices. Over 80% of the total area of the Panhandle fields is controlled by major pipeline companies (300 U. S. at 60). It would be possible for these companies to buy small amounts of gas from independent producers at a high Mcf price and accordingly claim that the price so paid represented the commodity value to which they were entitled in calculating the value of the gas which they produced themselves. "When the pipe-line interests control the only outlets to markets, an arbitrary setting of field prices seems inevitable."[28]

On the other hand, the cost system adopted by the Commission is fair alike to consumers and natural-gas companies.[29] It is readily apparent that if a field such as Panhandle or Hugoton

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[28] Federal Trade Commission Report No. 84–A, p. 133.

[29] Contrary to the contentions which petitioners advance on the basis of the tabulation in Appendix C to their brief, as we show in Appendix B of this brief, when actually computed, the allowed cost of gas produced by petitioners aver-

should be discovered near Chicago or Detroit, the cost of delivering gas from such field to those cities would be low and gas companies which were incurring higher transportation costs in delivering gas from distant points would be faced with bankruptcy if they were held to the commodity price.[30] On the other hand the Commission allows the acquisition costs of leaseholds, the delay rentals thereon while they are being held in reserve, well drilling and exploratory costs and all expenses incident to the operation of the gas leaseholds, including royalty payments. Thus the pipeline companies, whose business in the final analysis consists of the interstate sale of gas at wholesale, are assured of the cost of producing the commodity which they sell. Certainly, it may not be said that the action of the Commission in electing to use the cost rather than the commodity value of the gas lacks a rational basis. See *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 615–616. Indeed, since the Commission has established its policy of allowing cost of production, investors have been lending money at progressively lower rates (Exhibit 253, Charts Nos. 33 and 34, R. XIV, 6031, 6033). The average yield on bonds, debentures and notes issued

ages 3.75¢ per Mcf as compared with the 3.71¢ per Mcf average cost of gas purchased.

[30] It is significant to note that Hope Natural Gas Company purchased gas at prices lower than the cost of producing its own gas. See record in No. 34, Oct. Term 1943, II, 309, 312.

by natural-gas companies has declined from 4.59% in 1936 to 3.11% in 1941 (ibid.).

Finally, if the commodity price rather than cost were adopted by the Commission there would no longer be any necessity for treating the gas business as presenting any hazards peculiar. As a result, the transmission facilities, which constitute the larger portion of the pipe lines investment, would be entitled to a lower rate of return than 6½%.[31]

We accordingly submit that there was no requirement that the Commission, in fixing petitioners' rates for the interstate sale for resale of natural gas, should fix the cost of the gas so sold on a commodity rather than a cost of production basis.

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[31] If the return on petitioners' transmission facilities were limited to 5½% or 6%, the liberality of the return on their production facilities under the Commission's order is apparent:

	Return allowed on Production Property	
	If Other Property Entitled to 5½%	If Other Property Entitled to 6%
1. Rate base allowed	$67,137,305	$67,137,305
2. Deduct: Depreciated cost of production property (See Pet. Br. App. C)	2,555,473	2,555,473
3. Rate base—other property	64,581,832	64,581,832
4. Total return allowed	4,363,925	4,363,925
5. Return on property other than production property	3,552,000	3,874,910
6. Return on production property	811,925	489,015
7. Per cent of return allowed on production property	31.8%	19.1%

CONCLUSION

For the reasons stated, it is respectfully submitted that the decision below should be affirmed.

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JANUARY 1945.

APPENDIX A

The pertinent provisions of the Natural Gas Act of 1938, c. 556, 52 Stat. 821 (15 U. S. C. § 717 *et seq.*), as amended by the Act of February 7, 1942 (56 Stat. 83), are as follows:

> SECTION 1. (a) As disclosed in reports of the Federal Trade Commission made pursuant to Senate Resolution 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is hereby declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest.
>
> (b) The provisions of this act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.
>
> SEC. 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the

transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to

the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided*, That the Commission shall not have authority to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the

rate, charge, classification, or service goes into effect; the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

Sec. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in

connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however*, That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas.

SEC. 6. (a) The Commission may investigate and ascertain the actual legitimate cost of the property of every natural-gas company, the depreciation therein, and, when found necessary for rate-making purposes, other facts which bear on the determination of such cost or depreciation and the fair value of such property.

(b) Every natural-gas company upon request shall file with the Commission an inventory of all or any part of its property and a statement of the original cost thereof, and shall keep the Commission informed regarding the cost of all additions, betterments, extensions, and new construction.

SEC. 7. (c) No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefore, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: *Provided, however,* That if any such natural-gas company or predecessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on the effective date of this amendatory Act, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission within ninety days after the effective date of this amendatory Act. Pending the determination of any such application, the continuance of such operation shall be lawful.

In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: *Provided, however,* That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice or hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest.

(e) Except in the cases governed by the provisos contained in subsection (c) of this section, a certificate shall be issued to any qualified applicant therefore, authorizing the whole or any part of the operation, sale, service, construction, extension, or acquisition covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the Commission thereunder, and that the proposed service, sale, operation, construction, extension, or acquisition, to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. The Commission shall have the

power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require.

(f) The Commission, after a hearing had upon its own motion or upon application, may determine the service area to which each authorization under this section is to be limited. Within such service area as determined by the Commission a natural-gas company may enlarge or extend its facilities for the purpose of supplying increased market demands in such service area without further authorization.

(g) Nothing contained in this section shall be construed as a limitation upon the power of the Commission to grant certificates of public convenience and necessity for service of an area already being served by another natural-gas company.

SEC. 8. (a) Every natural-gas company shall make, keep, and preserve for such periods, such accounts, records of cost-accounting procedures, correspondence, memoranda, papers, books, and other records as the Commission may by rules and regulations prescribe as necessary or appropriate for purposes of the administration of this act: *Provided, however*, That nothing in this act shall relieve any such natural-gas company from keeping any accounts, memoranda, or records which such natural-gas company may be required to keep by or under authority of the laws of any State. The Commission may prescribe a system of accounts to be kept by such natural-gas companies, and may classify such natural-gas companies and prescribe a system of accounts for each class. The Commission,

after notice and opportunity for hearing, may determine by order the accounts in which particular outlays or receipts shall be entered, charged, or credited. The burden of proof to justify every accounting entry questioned by the Commission shall be on the person making, authorizing, or requiring such entry, and the Commission may suspend a charge or credit pending submission of satisfactory proof in support thereof.

(b) The Commission shall at all times have access to and the right to inspect and examine all accounts, records, and memoranda of natural-gas companies; and it shall be the duty of such natural-gas companies to furnish to the Commission, within such reasonable time as the Commission may order, any information with respect thereto which the Commission may by order require, including copies of maps, contracts, reports of engineers, and other data, records, and papers, and to grant to all agents of the Commission free access to its property and its accounts, records, and memoranda when requested so to do. No member, officer, or employee of the Commission shall divulge any fact or information which may come to his knowledge during the course of examination of books, records, data, or accounts, except insofar as he may be directed by the Commission or by a court.

(c) The books, accounts, memoranda, and records of any person who controls directly or indirectly a natural-gas company subject to the jurisdiction of the Commission and of any other company controlled by such person, insofar as they relate to transactions with or the business of such natural-gas company, shall be subject to ex-

amination on the order of the Commission.

SEC. 9. (a) The Commission may, after hearing, require natural-gas companies to carry proper and adequate depreciation and amortization accounts in accordance with such rules, regulations, and forms of account as the Commission may prescribe. The Commission may from time to time ascertain and determine, and by order fix, the proper and adequate rates of depreciation and amortization of the several classes of property of each natural-gas company used or useful in the production, transportation, or sale of natural gas. Each natural-gas company shall conform its depreciation and amortization accounts to the rates ascertained, determined, and fixed. No natural-gas company subject to the jurisdiction of the Commission shall charge to operating expenses any depreciation or amortization charges on classes of property other than those prescribed by the Commission, or charge with respect to any class of property a percentage of depreciation or amortization other than that prescribed therefor by the Commission. No such natural-gas company shall in any case include in any form under its operating or other expenses any depreciation, amortization, or other charge or expenditure included elsewhere as a depreciation or amortization charge or otherwise under its operating or other expenses. Nothing in this section shall limit the power of a State commission to determine in the exercise of its jurisdiction, with respect to any natural-gas company, the percentage rates of depreciation or amortization to be allowed, as to any class of property of such natural-gas company, or the composite depreciation or

amortization rate, for the purpose of determining rates or charges.

(b) The Commission, before prescribing any rules or requirements as to accounts, records, or memoranda, or as to depreciation or amortization rates, shall notify each State commission having jurisdiction with respect to any natural-gas company involved and shall give reasonable opportunity to each such commission to present its views and shall receive and consider such views and recommendations.

SEC. 10. (a) Every natural-gas company shall file with the Commission such annual and other periodic or special reports as the Commission may by rules and regulations or order prescribe as necessary or appropriate to assist the Commission in the proper administration of this act. The Commission may prescribe the manner and form in which such reports shall be made, and require from such natural-gas companies specific answers to all questions upon which the Commission may need information. The Commission may require that such reports shall include, among other things, full information as to assets and liabilities, capitalization, investment and reduction thereof, gross receipts, interest due and paid, depreciation, amortization, and other reserves, cost of facilities, cost of maintenance and operation of facilities for the production, transportation, or sale of natural gas, cost of renewal and replacement of such facilities, transportation, delivery, use, and sale of natural gas. The Commission may require any such natural-gas company to make adequate provision for currently determining such costs and other facts. Such reports shall be made

under oath unless the Commission otherwise specifies.

(b) It shall be unlawful for any natural-gas company willfully to hinder, delay, or obstruct the making, filing, or keeping of any information, document, report, memorandum, record, or account required to be made, filed, or kept under this act or any rule, regulation, or order thereunder.

SEC. 11. (a) In case two or more States propose to the Congress compacts dealing with the conservation, production, transportation, or distribution of natural gas it shall be the duty of the Commission to assemble pertinent information relative to the matters covered in any such proposed compact, to make public and to report to the Congress information so obtained, together with such recommendations for further legislation as may appear to be appropriate or necessary to carry out the purposes of such proposed compact and to aid in the conservation of natural-gas resources within the United States and in the orderly, equitable, and economic reduction, transportation, and distribution of natural gas.

(b) It shall be the duty of the Commission to assemble and keep current pertinent information relative to the effect and operation of any compact betwen two or more States heretofore or hereafter approved by the Congress, to make such information public, and to report to the Congress, from time to time, the information so obtained, together with such recommendations as may appear to be appropriate or necessary to promote the purposes of such compact.

SEC. 14. (b) The Commission may, after hearing, determine the adequacy or inadequacy of the gas reserves held or controlled

by any natural-gas company, or by anyone on its behalf, including its owned or leased properties or royalty contracts; and may also, after hearing, determine the property and reasonableness of the inclusion in operating expenses, capital, or surplus of all delay rentals or other forms of rentals or compensation for unoperated lands and leases. For the purpose of such determinations, the Commission may require any natural-gas company to file with the Commission true copies of all its lease and royalty agreements with respect to such gas reserves.

SEC. 16. The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this act. Among other things, such rules and regulations may define accounting, technical, and trade terms used in this act; and may prescribe the form or forms of all statements, declarations, applications, and reports to be filed with the Commission, the information which they shall contain, and the time within which they shall be filed. Unless a different date is specified therein, rules and regulations of the Commission shall be effective thirty days after publication in the manner which the Commission shall prescribe. Orders of the Commission shall be effective on the date and in the manner which the Commission shall prescribe. For the purposes of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different classes of persons or matters. All rules

and regulations of the Commission shall be filed with its secretary and shall be kept open in convenient form for public inspection and examination during reasonable business hours.

SEC. 19. (a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this act to which such person, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.

(b) Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of

the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be served upon any member of the Commission and thereupon the Commission shall certify and file with the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the

Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347).

(c) The filing of an application for rehearing under subsection (a) shall not, unless specifically ordered by the Commission, operate as a stay of the Commission's order. The commencement of proceedings under subsection (b) of this section shall not, unless specifically ordered by the court, operate as a stay of the Commission's order.

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APPENDIX B

Schedule 1, page 1

PANHANDLE EASTERN PIPE LINE COMPANY
COST OF GAS PRODUCED AT WELL HEAD
COMPARED WITH AVERAGE COST OF PURCHASED GAS
BASED ON THE FEDERAL POWER COMMISSION'S OPINION

Account		Commission Opinion: Total Cost	Commission Opinion: Operation of Wells & Leases
OPERATION AND MAINTENANCE			
Production Expense			
Gas Well Operation	(R. XII, 5595)	$ 59,495	$ 59,495
Gas Well Maintenance	"	19,087	19,087
Gas Well Royalties	"	171,044	171,044
Natural Gas Land Dept.	"	11,135	11,135
Delay Rentals	"	116,781	116,781
Field Line Operation	"	17,838	
Field Line Maintenance	"	8,036	
Sub-total	"	403,416	377,542
Natural Gas Purchased	"	1,180,918	
Gas Purchasing Expense	"	25,270	
Natural Gasoline Expenses	(R. XII, 5599)	202,587	
Transmission Expense	(R. XVI, 6885)	1,848,909	
Distribution Expense	"	9,069	
Customers' Acctg. & Coll. Exp.	"	28,760	
Sales Promotion Expense	"	32,724	
Administrative & General Expense	"	844,848	120,300 1/
Dupl. Charges - Gas Used in Oper., etc.	"	(749,889)	
Sub-total Oper. & Maint.	(R. XII, 5505)	3,823,612	
AMORTIZATION, DEPLETION AND DEPRECIATION			
Depletion of Producing Leases	(R. XII, 5505)	90,177	90,177
Amortization - Abandoned Leases	"	74,685	74,685
Depreciation	"	2,308,521	94,628 2/
Amortization - Gas Contracts	"	39,114	
Sub-total		2,512,497	
TAXES			
Production Taxes	(R. XII, 5591)	52,811	52,811
Other Taxes	(R. XII, 5505)	848,576	48,305 3/
Federal Income Tax	(R. I, 30)	1,093,768	54,142 4/
TOTAL OPERATING REVENUE DEDUCTIONS PER COMMISSION'S OPINION	(R. I, 31)	8,331,264	912,790
RETURN (6½% OF $67,137,305)	(R. I, 31)	4,363,925	215,672 5/
TOTAL COST OF SERVICE		$12,695,189	$1,128,462
M.C.F. of Gas Produced - 1941	(R. XII, 5567)		30,059,021
Average Cost per M.C.F. of Gas Produced - 1941			3.75¢
Average Cost per M.C.F. of Gas Purchased - 1941 ($1,180,918 divided by 30,157,409 MCF, R. XII, 5567)			3.71¢

NOTE: See Footnotes on Page 2.

PANHANDLE EASTERN PIPE LINE COMPANY

ALLOCATION OF GENERAL OVERHEAD, DEPRECIATION, TAXES AND RETURN TO WELLS AND LEASES

1/ Allocation of Gen. and Adm. Expense to Wells and Leases on basis of direct operating expenses:

	Total	Ratio	Gen. & Adm.
Wells and Leases	$ 377,542	14.29%	$ 120,300
Other Operation and Maint.	2,265,152	85.71%	721,546
Total, except purchased gas	$ 2,642,694	100.00%	$ 841,846

2/ Depreciation Expense Applicable to Wells:

Investment in Wells and Leases	$2,742,463
General Plant Applicable to Above	40,707
Depr. Base	$2,783,170
Depreciation rate for 1941 (Ex. IX, 4267)	3.4%
Depreciation for Wells and Leases	$ 94,628

3/ Property and Miscl. Taxes Applicable to Wells and Lease Allocated on basis of gross investment:

	Total	Ratio	Taxes
Wells and Leases	$ 4,508,240	5.716%	$ 48,505
Other Plant	74,361,067	94.284	800,071
Total	$78,869,307	100.000%	$ 848,576

4/ Allocation of Federal Income Tax on basis of earnings:

	Return	Ratio	Income Tax
Return on Wells and Leases	$ 215,672	4.95	$ 54,142
Return on Other Plant	4,148,253	95.05	1,039,626
Total Return at 6½%	$ 4,363,925	100.00	$1,093,768

5/ Allocation of Return:

	Rate Base	Rate of Return	Return
Net Investment Wells and Leases	$ 3,318,034	6.5%	$ 215,672
Net Investment Other Plant	63,819,271	6.5	4,148,253
Net Investment - Comm. Rate Base	$67,137,305	6.5	$4,363,925

Schedule 2

PANHANDLE EASTERN PIPE LINE COMPANY
NET INVESTMENT APPLICABLE TO WELLS AND LEASES
PER FEDERAL POWER COMMISSION OPINION

Plant Accounts	Commission Opinion Plant	Commission Opinion Depr. & Depl. Reserves	Net Investment Wells And Leases
Production Plant:			
Leases-Operated	1,017,[illegible]	[illegible]7,165	570,828
Leases-Unoperated	7[illegible]7,7[illegible]	[illegible]15,074	332,710
Sub-total Leases	1,765,777	862,239	903,538
Gas Wells and Equip.	2,7[illegible],163	[illegible]17,[illegible]	2,325,058
Total Wells and Leases	[illegible]	1,[illegible]	3,228,596
Refining Plant	70[illegible],26[illegible]		
Transmission and Gathering Plant	71,71[illegible],[illegible]06		
Distribution Plant	1[illegible],278		
Intangible and Undistributed Plant	20[illegible],71[illegible]		
Purchased Pipeline	[illegible]30,325		
Gas Sales and Purchase Contracts	35[illegible],997		
General Plant	71[illegible],15[illegible]		36,852 1/
Total Other Plant	7[illegible],361,067	11,317,3[illegible]	
Total Plant	7[illegible],[illegible]69,307	12,596,987	3,265,[illegible]7
Contributions In Aid of Constr.	([illegible],015)		
Working Capital	920,000		52,587 1/
Commission's Rate Base (A.L. 27)	7[illegible],7[illegible],292	12,[illegible],[illegible]7	3,31[illegible],034

Depreciation Reserve:	Plant	Ratio	Depr. Reserve
Wells and Equip.	2,7[illegible],163	3.557%	[illegible]17,[illegible]05
Other Plant	7[illegible],361,067	96.[illegible]%	11,317,343
Sub-total	77,10[illegible],[illegible]	100. %	11,7[illegible],7[illegible]8
Leases	1,765,777	Direct	862,239
Total Plant and Reserves	7[illegible],869,307		12,596,987

1/ Allocation of General Plant and Working Capital to Wells and Leases

	Total	Ratio	Applicable to Wells and Leases
General Plant	71[illegible],15[illegible]	[illegible].716	[illegible]0,707
Depr. and Amort. Reserve 15.22%	10[illegible],[illegible]90	[illegible].557	3,[illegible]55
Net Investment in General Plant	[illegible]		3[illegible],852
Working Capital	920,000	[illegible].71[illegible]	[illegible]52,587
	[illegible],52[illegible],76[illegible]		[illegible]

* Ratio of Wells and Leases to Total Plant is 5.716%

Ratio of Wells to Total Plant is 3.557%